



COLLEGE OF BUSINESS, PEACE, LEADERSHIP AND GOVERNANCE

AUDITING PRINCIPLES – MAC 305

END OF FIRST SEMESTER EXAMINATIONS

MARCH/ APRIL 2019

LECTURER: N. E CHIRIMA

DURATION: 3 HRS

INSTRUCTIONS

ANSWER **ALL** QUESTIONS

MARKS ARE SHOWN AT THE END OF EACH QUESTION

ANYTHING WRITTEN IN PENCIL IS DEEMED TO BE ROUGH WORK.

CREDIT WILL BE AWARDED FOR NEATLY PRESENTED WORK

START EACH QUESTION ON A NEW PAGE.

QUESTION 1 [25 marks]

You are an audit supervisor of Renee Audit firm and you are reviewing the documentation describing Tumirai and Sons' purchases and payables system in preparation for the interim and final audit for the year ending 30 June 2018. The company is a retailer of uniforms and has ten stores and a central warehouse, which holds the majority of the company's inventory.

Your firm has audited Tumirai and Sons for a number of years and as such, audit documentation is available from the previous year's file, including internal control flowcharts and detailed purchases and payables system notes. As far as you are aware, Tumirai and Sons' system of internal control has not changed in the last year. The audit manager is keen for the team to utilise existing systems documentation in order to ensure audit efficiency. An extract from the existing systems notes is provided below.

Extract of purchases and payables system

Store managers are responsible for ordering uniforms for their shop. It is not currently possible for store managers to request uniforms from any of the other nine stores. Customers who wish to order uniforms, which are not in stock at the branch visited, are told to contact the other stores directly or visit the company website. As the inventory levels fall in a store, the store manager raises a purchase requisition form, which is sent to the central warehouse. If there is insufficient inventory held, a supplier requisition form is completed and sent to the purchase order clerk, Oliver Dancer, for processing. He sends any orders above \$1,000 for authorization from the purchasing director.

Receipts of goods from suppliers are processed by the warehouse team, who agree the delivery to the purchase order, checking quantity and quality of goods and complete a sequentially numbered goods received note (GRN). The GRNs are sent to the accounts department every two weeks for processing.

On receipt of the purchase invoice from the supplier, an accounts clerk matches it to the GRN. The invoice is then sent to the purchase ordering clerk, Oliver, who processes it for payment. The finance director is given the total amount of the payments list, which she authorizes and then processes the bank payments. Due to staff shortages in the accounts department, supplier statement reconciliations are no longer performed.

Other information – conflict of interest

Renee Audit Firm has recently accepted the audit engagement of a new client, Kuku Ltd, who is the main competitor of Tumirai and Sons. The finance director of Tumirai and Sons has enquired how Renee Audit Firm will keep information obtained during the audit confidential.

Required:

- a) Explain the safeguards which Renee Audit Firm should implement to ensure that the identified conflict of interest is properly managed. 5 marks
- b) Explain the steps the auditor should take to confirm the accuracy of the purchases and payables flowcharts and systems notes currently held on file. 5 marks
- c) In respect of the purchases and payables system for Tumirai and Sons:
 - i. Identify and explain FIVE deficiencies;

- I. Recommend a control to address each of these deficiencies; and
- II. Describe a TEST OF CONTROL the auditor should perform to assess if each of these controls, if implemented, is operating effectively to reduce the identified deficiency.

15 marks

QUESTION 2 [25 Marks]

Bee Ltd is a multinational construction and property management company valued at \$US1.5BN, and it is listed on a major stock exchange. The company has formal presence in many major cities and construction projects around the world, ranging from road building, construction of public sector buildings, including hospitals, schools and university buildings to commercial contracts for office buildings. Some of the construction projects that Bee Ltd is involved with are financed by private finance initiative (PFI). Bee Ltd has a good reputation in this industry for quality and safety as well as its ability to deliver projects on time. These are all critical success factors for keeping its existing customers content and for providing a basis for winning future business. On its global website it has its publicly stated code of ethics and corporate values, which reflect best practice, as well as publicizing its Corporate Social Responsibility activities which include support in youth education, and in affected countries HIV/Aids outreach. Sara, a professionally qualified former colleague of yours from another country is joining Bee Ltd Community Divisions as a finance business partner. She contacts you to ask your advice regarding potential challenges and risks to ethical practice in your country. Discuss the questions below considering application of the Code of Ethics' fundamental principles.

- a) Outline threats and safeguards based on the fundamental principles of the Code. 5 marks
- b) What are the possible challenges, risks, threats and ethical pressures Sara may face in upholding her professional code? 8 marks
- c) What safeguards should be put in place? 7 marks
- d) What other support is needed? Where is it likely to come from? 5 marks

QUESTION 3 [25 Marks]

In February 2017 the directors of Han Eng suspended the managing director. At a disciplinary hearing held by the company on 17 March 2017 the managing director was dismissed for gross misconduct, and it was decided the managing director's salary should stop from that date and no redundancy or compensation payments should be made. The managing director has claimed unfair dismissal and is taking legal action against the company to obtain compensation for loss of his employment. The managing director says he has a service contract with the company which would entitle him to two years' salary at the date of dismissal. The financial statements for the

year ended 30 April 2017 record the resignation of the director. However, they do not mention his dismissal and no provision for any damages has been included in the financial statements.

Required

- i. Discuss whether or not and how (with reference to the appropriate International Accounting Standard) this event should be disclosed in financial report for the year ended 30 April 2017. 5 marks
- ii. Describe the audit procedures you will carry out to verify any contingent liabilities arising as a result of the MD's suspension. 10 marks
- iii. List and describe six financial statement assertions, other than completeness, used by auditors in the audit of financial statements. 6 marks
- iv. ISA 700 Forming an Opinion and Reporting on Financial Statements requires auditors to produce an audit report. This report should contain a number of consistent elements so that users are able to understand what the audit report means. Describe FOUR elements of an unmodified auditor's report and for each explain why they are included. 4 marks

QUESTION 4 [25 Marks]

- a) List and explain four factors that will influence the auditor's judgment regarding the sufficiency of the evidence obtained. 4 marks
- b) ISA 580 *Written Representation* provides guidance on the use of written representations as audit evidence. List six items that could be included in a representation letter. 3 marks
- c) After performing tests of controls, the auditor is of the opinion that audit evidence is not sufficient to support the audit opinion; in other words many control errors were found. Explain three actions that the auditor may now take in response to this problem. 3 marks
- d) Explain each of the five fundamental principles of the Professional Code of Conduct. 5 marks
- e) Explain the five threats to the auditor's independence as outlined by the Professional Code of Conduct. 5 marks
- f) Outline the purpose of planning an audit engagement, differentiating between the overall audit strategy and the detailed audit plan. 5 marks

END OF PAPER